NO. 74-529

MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1974

PAT RYAN & ASSOCIATES, INC.,

Petitioner,

vs.

OCCIDENTAL LIFE INSURANCE COMPANY OF NORTH CAROLINA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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NO.

PAT RYAN & ASSOCIATES, INC.,

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VS.

OCCIDENTAL LIFE INSURANCE COMPANY OF NORTH CAROLINA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in the above-entitled cause on May 8, 1974.

OPINIONS BELOW

The opinion of the Court of Appeals is officially reported at 496 F.2d 1255 (1974), is unofficially reported at 1973-74 CCH Fed. Sec. L. Rep. ¶94,551 (1974) and is printed at pages 1a-23a of Appendix A to this petition, *infra*. No District Court opinion has been reported. The opinions of the District Court that accompanied those of its orders that are pertinent to this petition are printed at pages 25a-36a of Appendix A to this petition, *infra*.

JURISDICTION

The judgment of the Court of Appeals was entered on May 8, 1974. A timely petition for rehearing was denied June 24, 1974. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

QUESTIONS PRESENTED

The decisions below raise two important questions of federal law that merit this Court's consideration because they have been resolved in conflict with decisions of this Court and other Courts of Appeals. We ask this Court to consider:

(1) Whether Section 29(b) of the Securities Exchange Act of 1934 precludes an action for breach of a contract for the sale of securities by a seller who, in violation of the Act, has defrauded the purchaser.

(2) Whether, by adopting an improper standard and procedure for review of a trial court order vacating a jury's damage award and ordering a new trial, the court below sanctioned a wrongful invasion of the province of the jury and a deprivation of petitioner's constitutional right to a trial by jury.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The constitutional provision involved in this case is Amendment VII to the Constitution of the United States.

The statutory provisions involved are Sections 10(b) and 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b) and 15 U.S.C. §78cc(b); and Rule 10b-5, promulgated under §10(b), 17 C.F.R. §240.10b-5.

These provisions are printed as Appendix B to this petition, *infra*.

STATEMENT OF THE CASE

Petitioner, a victim of fraud in the purchase of securities, seeks review in this Court of decisions below which held it liable to the seller in the net amount of $400,000 on the contract to purchase the stock involved. Denial to petitioner by the courts below of a statutory defense to the contract, and the validity of an order setting aside a jury's award of counterclaim damages in petitioner's favor are at issue.

In this litigation, Occidental Life Insurance Company of North Carolina sued the Petitioner, Pat Ryan & Associates, Inc. for breach of a contract arising out of the sale to Ryan of all of the stock of Virginia Surety Company, Inc., a wholly owned subsidiary of Occidental Life. Ryan counterclaimed for violations by Occidental Life of the federal securities laws in connection with the sale. The courts below specifically found that there was ample evidence to support the findings of two juries that Occidental Life had violated those laws. (A 11a, 31a.) [1]

The action was tried twice, and each time the District Court directed a verdict against Ryan on the complaint in the amount of $770,000. On the counterclaim, the first jury awarded Ryan $797,000; the District Court set that award aside and ordered a new trial. The second jury awarded Ryan only $379,000 and the trial court entered judgment for $400,000 in Occidental's favor. The Court of Appeals rejected the appeals of both parties and affirmed the judgment, except as to the award of interest.

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[1] Citations to the opinions and orders below that are printed in Appendix A to this Petition will appear herein as "A ....." Citations to the transcript of the first trial will appear as "Tr. I, Nov. 17, 1972, [e.g.] at ....." (References to dates of the first transcript are necessary because each day's copy is separately paginated.) Citations to the transcript of the second trial will appear as "Tr. II at ....."

The contract for the sale of the Virginia Surety stock called for a cash payment by Ryan of $1,527,000 at the closing in October, 1969, and execution by the parties of a reinsurance agreement that would provide Occidental Life $750,000 additional compensation for the sale over a three year period. This payment arrangement was reached as a compromise. Ryan viewed Occidental's asking price of $1,927,000 for the stock of Virginia Surety as more than the company was worth and was unwilling to pay that much for the stock. (Tr. I, Nov. 16, 1972, at 91-101.) However, the reinsurance agreement—under which Ryan was to produce insurance premiums for Occidental that it would have to produce for some carrier anyway in states where it was not licensed to write insurance directly[2]—established a continuing business relationship that would benefit Occidental in the amount of $750,000, but at no additional cost to Ryan. (A 3a.) Under the agreed arrangement, Ryan was able to purchase the stock for what it felt was a fair cash cost to it, and Occidental was put in the position of receiving additional compensation for the stock well above its asking price.

At the closing, the $1,527,000 payment was made to Occidental and the reinsurance agreement was signed. The controversy that would bring the parties before this Court began shortly thereafter. After the closing and continuing through the spring of 1970, Ryan learned of a number of important facts that had been misrepresented or concealed from it during negotiations for the sale and which bore directly on the value of the Virginia Surety stock.

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[2] Prior to the sale, Ryan was engaged in writing insurance in a limited number of states.

From a letter received shortly after the sale from the Connecticut Insurance Department revoking the license of Virginia Surety in that state, Ryan learned for the first time that examiners from the insurance departments of five states had conducted a tri-annual examination of Virginia Surety's condition in August and September of 1969, just weeks before the sale. (A 4a.) The report of that examination concluded that the financial statement of Virginia Surety of December 31, 1968, had underestimated the company's liabilities by over $600,000. The adjustment required to correct the error exhausted the company's surplus and impaired its capital as of that date. Virginia Surety accepted the report as written three days prior to the closing with Ryan. Not only had Occidental failed to inform Ryan during their negotiations that the examination of Virginia Surety had taken place, but the contract itself, written by Occidental, contained a provision disclaiming any knowledge on the part of Occidental of any governmental investigation which might adversely affect the sale. Furthermore, Occidental knew from the examination report that the December 31, 1968, financial statement of Virginia Surety it had provided Ryan was false and misleading. (Tr. I, Nov. 14, 1972, at 317.)

The revelations did not stop with the tri-annual examination report and the Connecticut license revocation. Ryan soon learned of restrictions that had been imposed prior to the sale on Virginia Surety's license to operate in North Carolina. Ryan also discovered that the previous owners of Virginia Surety had agreed with the insurance departments of Michigan and California that the company would write no further business in those states, in exchange for the licensing there of another Occidental subsidiary. Finally, the insurance department of Maryland followed Connecticut's lead and revoked Virginia's Surety license. (A 4a-5a.)

The discovery of these facts and their consequences made it apparent that the Virginia Surety stock was not the investment that had been bargained for. Ryan had wanted to purchase, as the court below noted, "an ongoing corporate enterprise with a good business reputation" (A 10a-11a); it did not get that.[3]

Accordingly, before beginning performance under the reinsurance agreement, Ryan sought to obtain compensation for the injuries that Occidental's actions had caused it. Occidental, however, rejected Ryan's attempt to settle the grievances amicably and, five months before Ryan's performance came due, initiated this lawsuit in the state court of North Carolina alleging failure to perform under the reinsurance agreement.

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[3] Although Occidental has attempted to minimize its misrepresentations and non-disclosures by focusing on the license difficulties alone, all expert witnesses—including those called by Occidental—agreed that the value of Virginia Surety had been significantly damaged far beyond the impairments to its licenses. For example, Richards D. Barger, former insurance commissioner of California and former President of the National Association of Insurance Commissioners, when asked his opinion of the effect of the adverse examination report on "future relationships with regulatory agencies of the States in which the company is licensed to do business," replied:

> Well, very unsalutory, very bad.
>
> . . . .
>
> [T]he taint of having its capital impaired . . . . persists for some period of time, depending upon the memories of the staff personnel of the insurance departments, notwithstanding whether the management changes or not. (Tr. II at 848-850.)

To the same effect was the testimony of Ralph F. Colton (Tr. II at 765-66), T. Nelson Parker (Tr. I, Nov. 15, 1972, at 112-15, 382-86), James Rutherford (Tr. I, Nov. 16, 1972, at 24-25), and Occidental witnesses Ernest A. Randolph (Tr. II at 1225-26) and Alfred J. Bohlinger (Tr. II at 1276-78).

After removing the action to the Federal District Court on grounds of diversity, Ryan filed an answer and counterclaim setting up the misrepresentations, omissions, and breaches that had occurred in connection with the sale of stock. The answer and counterclaim originally sounded in breach of contract and common law fraud, but later was amended to assert that the same fact allegations constituted violations of Sections 12(*2*) and 17(a) of the Securities Act of 1933, 15 U.S.C. 77*l*(2) and 15 U.S.C. 77q(a), and Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §240.10b-5.[4]

At the conclusion of the first trial, Ryan contended that the alleged violations of the securities laws and the prior breach by Occidental of the contract sued upon were a defense to the complaint. (Tr. I. Nov. 17, 1972, at 33-34.) The trial court rejected the contention and directed a verdict on the complaint in favor of Occidental, and against Ryan, in the amount of $770,000. The case was then submitted to the jury on the defendant's counterclaim, under instructions agreed to by both parties. (Tr. I, Nov. 17, 1972, at 147, 151.) The jury found in favor of Ryan in the amount of $797,000 in damages.

Two months later, the District Court entered an order that the verdict of the jury rendered in Ryan's favor on its counterclaim be set aside on the issue of damages because "so grossly contrary to the weight of the evidence as to be shocking to the conscience of the court." Its order did not particularize the grounds further. A new trial was

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[4] The District Court had jurisdiction of Occidental's breach of contract claim pursuant to 28 U.S.C. §1332(a) and jurisdiction of Ryan's claims under the federal securities laws pursuant to §22(a) of the Securities Act of 1933, 15 U.S.C. §77v(a), and §27 of the Securities Exchange Act of 1934, 15 U.S.C. §78aa.

ordered on all issues arising on the counterclaim, but the trial court refused to set aside its directed verdict in favor of Occidental on its complaint. (A 25a-26a.)

Ryan then filed a motion under Rule 54(b) for the entry of final judgment on Occidental's complaint so that an immediate appeal could be taken of the directed verdict. The District Court denied the motion, but it did set aside the verdict it had directed in Occidental's favor "upon further consideration in the light of the briefs subsequently submitted in connection with defendant's Rule 54(b) motion." (A 27a.) The case was then set for retrial on all the issues raised by the complaint, answer and counterclaim.

At the close of evidence in the second trial, the District Court again, however, directed a verdict against Ryan in the amount of $770,000 on Occidental's breach of contract claim. The jury again returned a verdict in favor of Ryan on the counterclaim but, acting pursuant to instructions changed from the first trial and objected to by Ryan (Tr. II, Apr. 28, 1973, at 137-153), the jury limited its verdict on the counterclaim to $370,000. The District Court entered judgment in favor of Occidental for the $400,000 difference between the court's directed verdict on the complaint and the jury's verdict on the counterclaim.

Both parties appealed the final judgment entered by the District Court. With the exception of a modification of the judgment with respect to the award of pre-judgment interest, the Court of Appeals affirmed. In its decision, the court below rejected Ryan's contentions that the District Court had committed reversible error in its new trial order following the first trial, in its damage instructions in the second trial, in directing a verdict in both trials in Occidental's favor on the complaint, and in denying Ryan the alternatively requested relief of rescission. Ryan's petition for rehearing was denied on June 24, 1974.

REASONS FOR GRANTING THE WRIT

This case presents two important issues for resolution by this Court, the first of which involves construction of §29(b) of the Securities Exchange Act of 1934. This provision declares void, as regards rights of the violator, contracts made in violation of that statute. The decision by the Court of Appeals below that §29(b) is not a contract defense overrides the statute, conflicts with decisions by the Courts of Appeals for the Seventh, Sixth, and Second Circuits, and ignores and misconstrues opinions of this Court. It has deprived Petitioner of a remedy clearly intended by Congress and has materially blunted the effectiveness of the Act.

The second issue involves Petitioner's constitutional right to a trial by jury and the question of the proper standard and procedure on review to be applied to a trial court's order setting aside a jury damage award and granting a new trial. The decision of the court below on this issue conflicts with those of the Courts of Appeals for the District of Columbia, Second, Third, Fifth, Sixth, and Eighth Circuits. This conflict and the important constitutional question of the amount of discretion allowed a trial court to vacate the findings of a properly-instructed jury because it would have weighed the evidence differently are ripe for resolution by this Court. The results below, we respectfully submit, appropriately call for exercise of this Court's power of supervision and its authority to settle the law.

I.

The Court of Appeals' Ruling That Section 29(b) of the Securities Exchange Act of 1934 Does Not Preclude an Action for Breach of Contract Against a Defrauded Purchaser of Stock Deprived Petitioner of a Remedy Expressly Provided by Congress.

As its first affirmative defense to Occidental's breach of contract complaint, Ryan set up the fraudulent misrepresentations and non-disclosures "more fully set forth in [its] counterclaim." Acting on the basis of what the lower court itself termed "ample evidence" (A 21a.), the juries in both trials concluded that the allegations of fraud were well-founded. But these issues were allowed to go to the jury only in connection with the counterclaim. With respect to Occidental's complaint, the trial court rejected Ryan's defense based on precisely the same operative facts and directed a verdict against it. The Court of Appeals affirmed.

We respectfully urge upon this Court that these rulings below cannot be squared with the unambiguous language of §29(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78cc(b), which provides that:

> Every contract made in violation of any provision of this chapter or of any rule or regulation thereunder . . . shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made . . . any such contract. . . .

In *dicta*, this Court declared in *Mills* v. *Electric Auto-Lite*, 396 U.S. 375, 387 (1970), that the above-quoted "language establishes that the guilty party is precluded from enforcing the contract against an unwilling innocent party. . . ." The court below, however, took the position that

"[w]e do not think §29(b) has such a devastating meaning." (A 16a.) That position, we respectfully submit, was wrong and should be corrected. Moreover, it reads out of the statute a specific remedy intended by Congress and is flatly contradictory to the Seventh, Sixth, and Second Circuits' construction of this provision.

In a case almost identical to this one, *Sundstrand Corp.* v. *Standard Kollsman Industries, Inc.*, 488 F.2d 807 (7th Cir. 1973), the Court of Appeals for the Seventh Circuit held that §29(b) *does* provide a defense to an action on a contract for the sale of securities to the victim of violations of Rule 10b-5. In that case, plaintiff alleged violations of the Rule in connection with the sale to it of an option to purchase stock of the corporate defendant. One of the individual defendants, the previous owner of the stock option, counterclaimed on a contractual monetary obligation obtained in connection with the sale to plaintiff of the stock option. After reversing the trial court's dismissal of the complaint, the Court of Appeals went on to consider the effect of the alleged 10b-5 violation on the counterclaim for breach of contract. Relying on §29(b), the court held that the counterclaimant would not be entitled to a hearing on his contract claim if the plaintiff were successful in proving "that the contract sued upon was made in violation of the Securities Exchange Act of 1933 [sic]. . . . Its defense to [the] counterclaim will rise or fall with the outcome of the retrial of its fraud claim. . . ." 488 F.2d at 816.

The instant case, like *Sundstrand*, involves countervailing claims by the buyer and seller of securities. The seller seeks to enforce the monetary obligations of a contract entered into in connection with the sale. The buyer seeks to recover damages due it because of the seller's violation

of §10(b) and Rule 10b-5 in connection with the stock sale, and raises the same facts as a defense to the seller's contract action. The decisions of the Courts of Appeals in the two cases simply cannot be reconciled.

The Court of Appeals for the Sixth and Second Circuits have also held that §29(b) provides a contract defense. *Goldman* v. *Bank of Commonwealth*, 467 F.2d 439 (6th Cir. 1972), and *Serzysko* v. *Chase Manhattan Bank*, 409 F.2d 1360 (2nd Cir. 1969), *cert. denied*, 396 U.S. 904 (1969), involved nearly identical fact situations. In each case, a borrower who had fraudulently induced the defendant bank to make loans in violation of Regulation U [5] sued to recover damages caused him by reason of the loans. Defendant bank in each case counterclaimed on the loan agreement. In both cases, the plaintiffs were denied recovery because of their own deceitful conduct. But in each case, §29(b) was held to provide a defense to the bank's counterclaim based on the loan contract.

The ruling by the court below also misapplies decisions of this Court and frustrates the congressional purpose underlying the Securities Exchange Act.

In concluding that §29(b) "is but a general provision which codified the common law principles already recognized in [*A. C. Frost & Co.* v. *Coeur D'Alene Mines Corp.*, 312 U.S. 38 (1941)]" (A 18a), the court below completely misreads *Frost*. In that case, this Court held that an option contract to purchase treasury stock was enforceable against the corporation, notwithstanding the fact that the shares were not registered. But the Court based its decision, at least in part, on the fact that "[n]o provision of

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[5] 12 C.F.R. §221 (1972), promulgated by the Board of Governors of the Federal Reserve System pursuant to §7(a) of the Securities Exchange Act of 1934, 15 U.S.C. §78g(a) (1970).

the act declares that in the absence of registration, contracts in contemplation of or having relation to a public offering shall be void." 312 U.S. at 41. Moreover, discussing the express remedies that *are* provided by the 1933 Act, this Court also stated that "the sanctions which Congress has definitely provided in order to insure obedience to the statute . . . must be given effect." *Id.* at 42. And the Court further noted that under the common law "whether a contract shall be enforced required consideration of the broad purposes of relevant statutes and the probable effect upon this. . . . [T]he end which Congress intended to accomplish was treated as the controlling factor." *Id.* at 44-45.

We submit that the decision below is squarely contrary to *Frost*. In *Frost* there was not an express statutory provision comparable to §29(b), which applies here. Moreover, in *Frost* it was the *violator* of the statute—the corporation which had failed to register its stock—which was seeking to hold the contract unenforceable; even under the terms of §29(b) the violator of the securities laws has no defense against a breach of contract action brought by the innocent party. Allowing the violator of the statute a contract defense under such circumstances would clearly have been contrary to the remedial purposes of the statute; a ruling in the corporation's favor would have encouraged future violations of the registration provisions. In the instant case, where it is the *victim* of securities fraud who seeks to defend against the contract, precisely the opposite is true.

The Court of Appeals below also offered support for its conclusions in quoting the following *dicta* from this Court's opinion in *Mills* v. *Electric Auto-Lite*, 396 U.S. 375, 387-88 (1970):

> This language establishes that the guilty party is precluded from enforcing the contract against an unwilling innocent party, but it does not compel the conclusion that the contract is a nullity, creating no enforceable rights even in a party innocent of the violation. The lower federal courts have read §29(b), . . . as rendering the contract merely voidable at the option of the innocent party. . . . This interpretation is eminently sensible. *The interests of the victim are sufficiently protected by giving him the right to rescind; to regard the contract as void where he has not invoked that right would only create the possibility of hardships to him or others without necessarily advancing the statutory policy of disclosure.* (A 17a; emphasis added by the court below.)

As we have discussed above, it is the *opening* sentence of this paragraph which states the general rule that we contend is applicable here. The language emphasized by the court below, we believe, was intended for application only to the unusual facts there presented—an attempt by minority shareholders to void a merger contract agreed to and not challenged by the majority. *Mills* simply does not support the Court of Appeals' elimination of the contract defense plainly intended by Congress to be part of the statute.

The court below also erred in concluding that, where other remedies are available, §29(b) need not be enforced because it might permit the purchaser "an unexpected windfall the amount of which depends on the fortuitous factor of how much of a down payment has been made." (A. 19a.) First, the statute does not state that §29(b) applies only in the absence of other remedies. Second, the holding is at odds with the rule in *Janigan* v. *Taylor*, 344 F.2d 781, 785 (1st Cir. 1965), *cert. denied* 382 U.S.

879 (1965), that, "it is more appropriate to give the defrauded party the benefit even of windfalls than to let the fraudulent party keep them." Third, enforcement of §29(b) according to its terms would not, as the Court of Appeals seemed to fear, dictate that a purchaser could keep the stock without paying for it. Rather, the court would certainly have an option in the appropriate case of allowing recovery of the actual value of the stock sold, minus any profit to the defrauding seller. In *Goldman* v. *Bank of Commonwealth, supra,* the court fashioned just such a remedy; while the bank was not allowed to enforce the loan agreement because of its own violation of the Act, it was allowed to recover the amount loaned without interest.

In contrast, what has occurred in this case is a clear example of why §29(b) should be literally applied to discourage fraudulent acts by sellers. In cases such as this one, where the victimized purchaser discovers the fraud prior to completing performance under the sales contract, the violator should not be permitted automatically to enforce the terms of that contract, thereby imposing upon the purchaser the burden of proving what is in effect a "set-off".

However, under the rule announced below, and given the uncertainties inherent in litigation, the defrauding seller may still gain more than he would have had he sold the stock with full and truthful disclosure; at worst, he retains the fair market value of the stock. He has then violated the Act without risk or peril; this cannot be what Congress intended but it is precisely what happened here.

As the judgment now stands, Ryan has been forced to pay Occidental's full asking price for the stock and Occidental has been allowed to reap a substantial profit from the sale despite its fraud.[6] The allowance of such a profit is directly contrary to basic securities law policy, as recognized by this Court in *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). In that case, brought by defrauded sellers of securities, the Court ruled that in "the situation where the defendant received more than the seller's actual loss," the defrauded seller's "damages are the amount of the defendant's profit." 406 U.S. at 155. We believe that the principle recognized in *Affiliated Ute* —that a violator of the securities laws may not be allowed to profit from its fraud—is applicable to the instant situation.

By its ruling in this case, the Court of Appeals has held in effect that Ryan acted improperly, that the innocent purchaser of stock from a seller who committed securities fraud in the sale cannot defend against the seller's suit on the sales contract, but must complete his performance and thereafter sue for damages or rescission. The effect of this ruling cannot, we submit, be reconciled with the

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[6] In footnote 9 to its opinion, the court below indicated that its ruling on §29(b) was based in part on the fact that it was not "disposed" to grant Ryan a right equivalent to the right to rescind, which was denied Ryan because of what the court described as Ryan's "dilatory action." (A 20a.) We submit that Ryan—by refusing to begin performance under the reinsurance agreement upon learning of the fraud until Occidental agreed to make recompense—as effectively invoked the right provided by §29(b) to void the contract sued upon as if it had uttered the magic incantation, "I rescind."

remedial purposes of the antifraud provisions of the securities laws.[7]

II.

By Adopting an Improper Standard and Procedure for Review, the Court Below Sanctioned a Wrongful Invasion of the Province of the Jury and Deprived Petitioner of Its Constitutional Right to a Trial by Jury.

The court below limited its review of the trial court's order setting aside the jury verdict "to ascertaining whether the decision amounts to an abuse of discretion," (A 12a) and, in concluding there had been no abuse, it relied on evidence adduced only at the second trial. In so doing, we submit, the Court of Appeals erroneously applied a much less exacting standard of review than that applied by the other Courts of Appeals under the same circumstances. The court's refusal to disturb the trial

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[7] The result reached by the Court of Appeals means that a defrauded purchaser of stock, supposedly the object of special protection by the securities laws, has *fewer* remedies available to him than would the defrauded purchaser of some other item. §2-717 of the U.C.C. provides:

> The buyer on notifying the seller of his intention to do so may deduct all or any of the damages resulting from any breach of contract from any part of the price still due under these same contracts. Gen.Stat.N.C. §25-2-717 (1965).

§2-721 of the U.C.C. provides:

> Remedies for material misrepresentation or fraud include all remedies available under this article for non-fraudulent breach. Neither rescission or a claim for rescission of the contract for sale nor rejection or return of the goods shall bar or be deemed inconsistent with a claim for damages or other remedies. Gen. Stat.N.C. §25-2-721 (1965).

court's rejection of a jury verdict that was reasonable, fully supported by the evidence, and wholly just has created a precedent that seriously jeopardizes a litigant's fundamental right to a trial by jury.

The court below completely failed to grasp the important distinction between a trial court's denial of a motion for a new trial and the grant of such a motion on the grounds that the size of the jury verdict is contrary to the weight of the evidence. However, other Courts of Appeals in recent years have recognized this vital distinction and the constitutional implications involved.

In prior cases in which trial courts have denied new trial motions or have granted new trials because of some kind of trial error—the Courts of Appeals have been reluctant to find a reversible abuse of discretion. This reluctance is understandable; a trial court ordering a new trial because of some legal error is exercising its authority as arbiter of the law, and a trial court refusing to disturb a jury's verdict is upholding the jury's function as trier of fact.

But when confronted with the grant of a new trial by a District Court because the verdict was felt contrary to the weight of the evidence or the damage award was thought excessive, as is the case here, the Courts of Appeals have enforced a much stricter standard. In such cases, the reviewing courts have held themselves duty bound to examine closely the action of the trial court in vacating findings of fact returned by the jury. Such close supervision by an appellate court is necessary "to protect the litigants' right to jury trial," since, in rejecting the jury's verdict, the "judge takes over, if he does not usurp, the prime function of the jury as the trier of the facts." *Lind* v. *Schenley*

Industries, Inc., 278 F.2d 79, 90 (3rd Cir. 1960), *cert. denied*, 364 U.S. 835 (1960). Accord, *Fireman's Fund Insurance Co.* v. *Malco Wrecking Co., Inc.*, 466 F.2d 179, 186-7 (8th Cir. 1972), *cert. denied*, 410 U.S. 930 (1973); *Grove* v. *Dun & Bradstreet, Inc.*, 438 F.2d 433, 438 (3rd Cir. 1971), *cert. denied*, 404 U.S. 898 (1971); *Duncan* v. *Duncan*, 377 F.2d 49, 52 (6th Cir. 1967), *cert. denied*, 389 U.S. 913 (1967); *Berner* v. *British Commonwealth Pacific Airlines*, 346 F.2d 532, 541 (2nd Cir. 1965), *cert. denied*, 382 U.S. 983 (1966).

These decisions by the Courts of Appeals follow the general principles expressed in the opinions of this Court regarding the sanctity of the jury's fact-finding role and the duty of the courts to "jealously guard" a litigant's right to a jury trial. *Jacob* v. *New York*, 315 U.S. 752, 753 (1942). In *Tennant* v. *Peoria & Pekin Union Ry. Co.*, 321 U.S. 29, 35 (1944), for example, this Court made clear, in its reversal of a Court of Appeals' decision setting aside a jury verdict, that a court's freedom to overturn a jury's conclusions of fact is limited indeed:

> It is the jury, not the court, which is the fact-finding body. It weighs the contradictory evidence and inferences, judges the credibility of witnesses, receives expert instructions, and draws the ultimate conclusion as to the facts. The very essence of its function is to select from among conflicting inferences and conclusions that which it considers most reasonable. [citations omitted]. That conclusion, whether it relates to negligence, causation or any other factual matter, cannot be ignored. Courts are not free to reweigh the evidence and set aside the jury verdict merely because the jury could have drawn different inferences or conclusions or because judges feel that other results are more reasonable.

Taylor v. *Washington Terminal Company*, 409 F.2d 145 (D.C. Cir. 1969), *cert. denied*, 396 U.S. 835 (1969), illustrates the principles that should have been applied below and the conflict among the circuits. In *Taylor*, the trial court found the jury's damage award of $80,000 excessive and granted the defendant's new trial motion; at the second trial, the jury awarded plaintiff only $25,000. The Court of Appeals, noting the importance of the role of the jury as fact-finder, evaluated the conflicting evidence and found that the jury could have reasonably returned a verdict for the larger amount. The court reversed and ordered the entry of judgment on the verdict returned at the first trial, holding that "where . . . it is clear that the jury has stayed within the reasonable range, the deference due its findings of fact outweighs the deference due the trial judge's first hand review of the evidence." 409 F.2d at 149.

The Sixth Circuit Court of Appeals has in two recent cases adopted and applied this same rule—that an appellate court "will . . . 'reverse the grant of a new trial for excessive verdict only where the quantum of damages found by the jury was *clearly* within "the maximum limit of a reasonable range." ' (emphasis in original)." *Manning* v. *Altec, Inc.*, 488 F.2d 127, 133 (6th Cir. 1973), quoting from *Taylor; Brewer* v. *Uniroyal, Inc.*, 1974 Trade Cas. ¶75,127, at p. 97,047 (6th Cir. 1974). *Cf. Gorsalitz* v. *Olin Mathieson Chemical Corporation*, 429 F.2d 1033, 1046-47 (5th Cir. 1970), in which the Fifth Circuit reversed a trial court's grant of remittitur because it was greater than the amount which would have reduced the damages awarded to "the maximum which the jury could reasonably find."

Not only did the court below apply an improper and conflicting standard of review on the new trial issue, it af-

firmed on the basis of its construction of testimony that was not in the record at the time of the trial court's decision but appeared only in the record of the second trial.

In conflict with this procedure, other Courts of Appeals examining the propriety of a trial court's grant of a new trial have restricted their examination of the record to what was before the trial court at the time of its decision. Thus, in *Hourstan* v. *Harrlan*, 457 F.2d 1105, 1107 (3rd Cir. 1972), the Court of Appeals for the Third Circuit, in considering on appeal from a second trial a claim that the trial court had erroneously granted a new trial on the grounds that the first trial verdict was contrary to the weight of the evidence, ruled that "only the events of that first proceeding as they related to the court's order need be evaluated." And the Court of Appeals for the Sixth Circuit, dealing with the same situation in *Duncan* v. *Duncan*, *supra*, based its decision on "the facts as developed at the first trial." 377 F.2d at 50.

Examination by this Court of what transpired in the first trial demonstrates clearly, we submit, that the Court of Appeals applied an improper standard and procedure for review. Such scrutiny is necessary because the trial court gave no explanation for its conclusion that the first trial evidence was insufficient to support the jury's damage award and the opinion of the Court of Appeals fails to provide the appropriate "detailed appraisal of the evidence bearing on damages." See *Grunenthal* v. *Long Island R. Co.*, 393 U.S. 156, 159 (1968).

At the close of the evidence in the first trial, jury instructions on the issues raised by Ryan Associates' counterclaim were given by the court as approved by both parties. After finding that Occidental had violated the antifraud provisions of the federal securities laws, the jury went on to compute damages in a way that adhered completely to the agreed-upon formula given in the court's

instructions. Assuming the evidence submitted on behalf of Ryan on damages was believed, the jury was in fact *required* by the instructions of the court to return a verdict for exactly the amount awarded.

The instructions on damages were clear:

> The measure of damages . . . is the difference between what the defendant in this case, Pat Ryan and Associates, agreed to pay for 6,000 shares of Virginia Surety Company stock, and what this Virginia Surety Company stock was worth to a willing and prudent investor, knowing all of the facts about Virginia Surety at the time it was purchased by the defendant. (Tr. I, Nov. 17, 1972, at 140-41.)

Given the District Court's subsequent instructions to the jury that it was to consider that Ryan had agreed to pay $2,297,000 for the stock of Virginia Surety, the jury's only remaining task was to determine what the stock was actually worth at the time it was sold to Ryan, and to award the difference in damages.

The testimony of expert witness James Rutherford was that, given the infirmities of the company (which had been misrepresented or concealed), the stock of Virginia Surety was worth no more than $1,500,000. (Tr. I, Nov. 16, 1972, at 54-55.) The difference between this figure and the figure that the jury was instructed to consider that Ryan Associates had agreed to pay was $797,000, precisely the amount awarded by the jury in damages.

Moreover, the jury's valuation of the Virginia Surety stock at $1,500,000 was supported by substantial other evidence in the first trial record. Occidental vice-president Robert Marshall, a former officer and director of Virginia Surety, testified that he considered $1,500,000 a "fair price." (Tr. I, Nov. 14, 1972, at 335.) Occidental chairman R. P. Woodson testified that Occidental Life had itself

purchased the stock from its subsidiary Occidental Fire & Casualty at approximately that price shortly before the sale to Ryan. (Tr. I, Nov. 15, 1972, at 22.)

In view of the explicit instructions on the measure and computation of damages and the considerable evidence supportive of the jury's action thereon, the conclusion of the District Court that the verdict on damages was "grossly contrary to the weight of the evidence" (A 26a) was, we respectfully submit, untenable and would have been reversed had the Court of Appeals applied the proper standard and procedure for review.

Furthermore, not only did the court below improperly base its affirmance of the new trial order on testimony adduced only in the second trial, but it completely misapplied that evidence.

To justify its decision, the court below stated that "[Ryan's] own experts testified that the difference in value of Virginia Surety because of the defects amounted to about $200,000," and that "[t]his amount constituted the major portion of [Ryan's] damages." (A 12a.) But the difference between the actual value of the stock of Virginia Surety and what the stock would have been worth had the company been free of defects has absolutely no relation to Ryan Associates' damages.

Ryan did not sue for the injury done to Virginia Surety by the mismanagement of the company by its former owners. Rather, Ryan Associates has sought to recover the damage it suffered as a *purchaser* by Occidental's fraudulent action in connection with the sale of stock. The correct measure of that damage is not what it would take to make Virginia Surety whole, but the difference between the price Ryan was required to pay and the actual value of the stock. *Estate Counseling Service, Inc.* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 303 F.2d 527, 533

(10th Cir. 1962); see also *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 155 (1972).

In many cases, of course, there would be no difference in these two measures. But here, the defrauded purchaser agreed to a purchase price far in excess of the value of the stock, in return for an arrangement (the reinsurance agreement) under which a major portion of the price could be satisfied by a transfer of business to the seller rather than with cash. The seller's preemptory suit on the contract and the trial court's directed verdict against Ryan forced the transaction into a straight cash deal at a figure far above the asking price that the buyer had at the outset rejected as excessive. As a result, the defrauded party has been left with only partial compensation for its loss and the seller has been handsomely rewarded for its fraud.[8]

In any event, the expert testimony as to "difference in value" upon which the court below has relied must be considered in context of earlier testimony by the same expert, Ralph Colton. He testified that the actual value of the stock of Virginia Surety was $1,466,000 and that the value of the charter and licenses of Virginia Surety would theoretically have been increased from $350,000 to about $560,000 to $600,000 if the company had been defect-free. (Tr. II at 771-74.) Thus, Colton's testimony can only be viewed as an expression of his opinion that the hypothetical defect-free company would have been worth $200,000

[8] This unjust second trial result was caused, we submit, by the trial court's insertion into the charge on damages, over Ryan's objection, of a description of the proper measure of damages as being equal to the "diminution in value" of the stock of Virginia Surety due to Occidental's fraud. The Court of Appeals refused to find prejudicial error in this portion of the trial court's charge.

more, or about $1.7 million; his testimony was not, as the court below erroneously observed, that "the difference [$200,000] . . . constituted the major portion of [Ryan's] damages." (A 12a.) Since Ryan was required by the directed verdict to pay not $1.7 million but $2,297,000 for the stock, the court manifestly understated Ryan's loss in the transaction.

In sum, the decision by the Court of Appeals upholding the trial court's grant of a new trial has deprived Ryan of a reasonable and proper jury verdict on the question of the amount of his damages in a way that seriously jeopardizes the constitutionally protected right to trial by jury. In order to preserve that right, this Court should grant review.

CONCLUSION

For the reasons set forth above, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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